

## **Dhan ki Baat #3 – Direct Index Funds are best**

### **Why Direct Index Funds are Best ?**

You can save around 2% a year by using Direct Index Funds. Index funds have started outperforming most active funds as in USA.

Some active funds and PMS (Portfolio Management Schemes) may justify the fees they charge but finding active funds who consistently beat index funds is hard.

Please spend a few minutes reading this note. We started with the conclusion.

### **Direct Funds are better than Regular Funds**

Direct funds were introduced on Jan 1, 2013 and now six years later many mutual fund investors are moving out of regular funds to direct funds. As the data below shows that over ten years an investor lost Rs 27308 on Rs 100000 or 27.30%. The difference is 0.75% per year but it grows because of Power of Compounding (Dhan ki Baat #2)

### **Index Funds are better than active funds**

They cost less and while in the past actively managed funds beat index funds justifying the higher fees the situation has changed over the last three years. See the data below:

For every lac invested in a ten-year period an active fund did Rs 133595 or 133.60% better, so it made sense to pay the higher feed for active funds.

For every lac invested in a three-year period an index fund did Rs 7935 or 7.94% better, so it made no sense to pay the higher fees for active funds. The fee difference was 1.86% per year while the performance differential was 2.68% so for this particular active fund the active fund selection was worse than the passive fund selection.

### **Direct Index Funds – Save 1.86%**

If you invest in a regular actively managed fund like SBI Blue Chip Growth, it costs 1.96% a year.

Switch to the direct version of the same fund it costs 1.21% (You save 0.75% every year)

An Index fund HDFC Index Fund Sensex Plan Direct Growth costs 0.1% (You save 1.86 % every year)

## **Direct Index Funds – Performance Ten Years**

If you pay more fees and the performance net of fees is better than it makes sense to pay more.

If you invested Rs 100000/- (one lac) on January 1, 2009 and redeemed it on January 1, 2019 you received money as below

SBI Blue Chip Direct Growth - Rs 512484 (Multiple – 5.12)

SBI Blue Chip Growth – Rs 485176 (Multiple – 4.85)

HDFC Index Sensex Direct Growth – Rs 378889 (Multiple – 3.79)

## **Direct Index Funds – Performance Three Years**

If you pay more fees and the performance net of fees is worse than it makes no sense to pay more fees

If you invested Rs 100000/- (one lac) on January 1, 2016 and redeemed it on January 1, 2019 you received money as below

HDFC Index Sensex Direct Growth – Rs 143179 (Multiple -1.43)

SBI Blue Chip Direct Growth - Rs 135244 (Multiple – 1.35)

SBI Blue Chip Growth – Rs 130729 (Multiple – 1.31)

## **Financial Literacy Nuggets**

Dhan ki Baat messages give you nuggets that you can study to improve your financial literacy. Lookout for the next message on “Dhan ki Baat”.